Testimony by Paul S. Hewitt
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Senate Select Committee on Aging
on
Global Aging: *Opportunity or Threat for the U.S. Economy?*
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Mr. Chairman, thank you for your leadership in scheduling this hearing on the opportunities and threats of global aging. I would be remiss if I did not also acknowledge the contributions of Senators John Breaux and Chuck Grassley and Judd Gregg to the CSIS Commission on Global Aging, which has been examining this question for three years now. The Commission also included three senior House Members; the former prime ministers of Japan, Italy, and India; and five current or former cabinet ministers; plus leading experts from international organizations and the private sector. Former Vice President Mondale was our first chairman.

The Commission's central finding was that the challenge posed by global aging is pervasive. It will affect everything from individual life plans to international security alliances. Global aging will generate important economic opportunities. But it will also create unprecedented dangers. Which of these forces triumphs will depend, in no small measure, on the course of policy reform over the next few years—not just in the U.S., but in countries the world over.

It will surprise some to learn that America will probably age less over the next 50 years than any other country except, possibly, Luxemburg. The Census Bureau projects that that our median age will rise by just 3.6 years—barely half the rate of the previous 50 years. The median age of the world is on track to rise by 9.7 years over this period, while the typical Mexican at mid-century will be 16.2 years older than her counterpart of today. As shown in Table 1, America's age structure will be converging with that of the developing world and diverging from those of our allies.

Table 1
Change in Median Age for Selected Countries and Groupings, 2000 to 2050

	U.S.	LDCs	World	Europe*	Japan	China	India
2000	35.5	18.2	26.5	37.7	41.2	30.0	23.7
2050	39.1	26.5	36.2	49.5	53.1	43.8	38.0
Increase	3.6	8.3	9.7	11.8	11.9	13.8	14.3

Source: United Nations; Census Bureau for U.S.
* Includes all Europe plus Russia (47 countries)

Population aging—driven by falling birthrates—is creating important opportunities in the developing world. In a phenomenon known as the "demographic bonus," falling child dependency directly increases per capita incomes, even as it frees women to participate in the labor market and enables families to spend more on health and education. The result can be a virtuous circle of economic growth and political stability.

Yet in order to capitalize on this bonus, societies must also provide employment. Without jobs, growing labor pools translate into ballooning legions of unemployed, who, in turn, are a source of social unrest. It was the recognition that unemployment had been the root of so much upheaval in the first half of the 20th century that led every industrial country to establish generous welfare states in the aftermath of World War II. Owing to their high costs, safety nets in the low- and middle-income countries are likely to be modest for the foreseeable future. This means that social peace in these regions will depend perilously on the state of the global economy.

Of particular concern, then, is the fact that aging is increasing the potential for crisis throughout the developed world. As shown in Table 2, CSIS estimates that by 2040, today's old-age benefit promises will consume an additional 12 percent of GDP a year in the typical developed country. Were these imbalances permitted to accumulate, by the mid-2020s, budget deficits in the rich countries would consume all of their savings, making them dependent on capital flows from the third world to fund domestic investment. Long before this happens, of course, capital shortages and default risks would spill over and disrupt growth everywhere.

Table 2
Percent Change in Old-Age Outlays in 12 Countries
Over 2001 Spending Levels

	2010	2020	2030	2040
Australia	1.0%	3.2%	5.2%	6.9%
Belgium	1.3%	4.7%	9.2%	12.0%
Canada	2.3%	6.4%	11.0%	14.0%
France	2.8%	7.4%	11.3%	13.8%
Germany	0.3%	2.9%	7.5%	10.2%
Italy	1.8%	5.1%	9.6%	12.9%
Japan	4.4%	7.6%	10.1%	14.8%
Netherlands	2.0%	5.5%	9.4%	12.3%
Spain	1.2%	4.4%	10.9%	19.5%
Sweden	1.3%	3.4%	6.0%	8.0%
UK	0.4%	1.3%	3.3%	4.3%
U.S.	1.9%	6.3%	10.1%	12.0%

CSIS Aging Vulnerability Index (2003)

A complete discussion of these estimates can be found in the *2003 Aging Vulnerability Index*. Mr. Chairman, I would like to request that a copy of this report be inserted into the record as an appendix to my testimony.

As dismal as these figures are, flagging economic growth could make matters worse. Surging labor forces have accounted for roughly half of all GDP growth in the developed world over the last 25 years. Yet the Organization for Economic Cooperation and Development estimates that shrinking labor forces will cut GDP growth by an average of -0.7 percent a year in Japan and -0.4 percent in the EU-15 during next 25 years. Even if productivity continues rising at past rates, GDP growth in both regions will fall under 1 percent by 2020—and in fast-aging Japan, Italy and Spain, worsening labor shortages will produce semi-permanent aging recessions.

More immediate, and worrying, are the effects of depopulation on product markets. In Germany and Japan, shrinking numbers of older and thriftier consumers already are creating overcapacity in industries, from construction to retail, that used to be engines of economic growth. The loss of pricing power in these sectors not only has been deflationary, but fiscally destabilizing, as collapsing corporate profits and rising bank losses have deprived governments of needed corporate income tax revenues. If demographic rather than cyclical factors are behind the malaise in Japan and Germany, as I believe they are, then the era of aging recessions may already have begun.

It remains that the industrial world's aging need not deprive developing countries of their demographic bonuses. Slowing growth in the rich countries will translate to fewer profitable opportunities for domestic investment. In response, managers of capital increasingly will look abroad to developing countries with large labor forces and low productivity, where infusions of technology and know-how can generate outsized returns. In this win-win scenario, rich country retirees would maintain high rates of return on their nest eggs while helping to accelerate economic development in the poorer regions.

This is already happening on a modest scale, mostly in the form of direct investment by multinational corporations. But much larger capital flows will be necessary if foreign investment is to play a meaningful role in developed world retirement finances. Maximizing this potential will require an historic expansion of global trade and investment alongside fundamental structural reforms in both the developed and developing regions. The rich countries will need to place much more of the retirement burden on saving—for example, by expanding private pensions—to ensure that they remain capital exporters. For their part, the developing counties must create the physical, educational, financial and legal infrastructure needed to become safer, more productive places to invest. Last, but not least, any aging strategy built around global synergies will require a stable geopolitical environment.

This brings us to a second demographic threat. Exploding unemployment and radicalism in the world's most youthful regions could wreck global prosperity by throwing "sand in the gears of cross-border connectivity," in the words of Stephen Roach.

Social scientists disagree on whether extreme youth is a precursor of conflict. After all, many young societies are peaceful, from Botswana to Bangladesh. Yet it remains that youth gluts characterize the world's hot spots: 16 of the 25 youngest countries have experienced major civil conflicts since 1995. Nor is it sheer coincidence that radical Islam flourishes in Palestine (median age of 16.8 in 2000), Saudi Arabia (18.4), Afghanistan (18.1), Iraq (18.8), and Pakistan (18.9), where the typical citizen is a teenager. Any comprehensive theory of global conflict will reflect that the 20th century's bloodiest upheavals, from Europe's Great War to China's Cultural Revolution, began with surpluses of teenagers.

During the next three decades, labor pools will grow by 146 million in the Arab world, and 402 million in Sub-Saharan Africa—with most of these gains coming in the volatile 15-30 age group. Rising unemployment and falling per capita incomes are a foregone conclusion. At the very least, the coming decades will see massive migration from these impoverished regions to an enfeebled and depopulating Europe still obsessed with its own ethnic purity. At the worst, financial shocks from deteriorating welfare state finances and political shocks from ballooning third world unemployment will feed on one another, creating an era of turmoil from which none of our social compacts will emerge intact.

Mr. Chairman, the era of global aging is underway. It is shaping such seemingly disparate events as deflation in Japan, financial flows to China, and the rise of radicalism in the Middle East. Managing this transition will require an extraordinary degree of policy coordination across national borders. In the best of all worlds, America will be the pivot point in this transition. We will serve as a bridge between a younger third world that must soon become the engine of global economic growth, if there is to be global growth, and aging Japan and Europe, whose leaders must discover prodigious reserves of political will, if their creaking welfare states are not to collapse and drag the rest of the world into economic and political chaos.

Leading the global aging transition will require more than favorable demographics, a large military, and economic and cultural primacy. It will require us to articulate to a wider, and frequently skeptical, world not simply the threats posed by the aging challenge, but the opportunities as well.